

Message Text

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ACTION ARA-14

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COME-00 DODE-00 EB-08 DOE-11 H-01 INR-10 INT-05
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SP-02 SS-15 STR-07 TRSE-00 ACDA-12 /121 W
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R 032210Z MAR 78
FM AMEMBASSY QUITO
TO SECSTATE WASHDC 7500
INFO AMCONSUL GUAYAQUIL

C O N F I D E N T I A L SECTION 1 OF 2 QUITO 1357

E.O. 11652: GDS
TAGS: ECON, ENRG, EC
SUBJECT: SPECIFICS OF GOE PLAN TO RAISE PRICES OF PETROLEUM

REF: QUITO 1361

SUMMARY: THE GOE FINANCE MINISTER HAS LAUNCHED A CAMPAIGN TO PREPARE PUBLIC OPINION FOR A SHARP RISE IN PRICES OF PETROLEUM DERIVATIVES, IN ORDER TO SUBSTANTIALLY REDUCE THE GOE'S SUBSIDIES ON THESE WHICH ARE NOW COSTING SOME \$200 MILLION ANNUALLY (EQUIV.). THE MINISTER CONFIDED TO AN EMBOFF THAT THE MILITARY IS DETERMINED TO EFFECT THESE PRICE RISES BEFORE LEAVING OFFICE, DESPITE THE FIERCE HISTORICAL OPPOSITION OF TRANSPORT UNIONS, LEFTIST STUDENTS AND OTHER ELEMENTS. THE RISES WILL NOT BE EFFECTED IN A SERIES OF PERIODIC SMALL INCREASES, HE SAID, BUT RATHER WILL BE A NOE-TIME LARGE INCREASE, WITH, HOWEVER, CONCESSIONAL RATES FOR PUBLIC TRANSPORTATION ENTITIES AND FOR PROFESSIONAL DRIVERS OF BUSES AND TAXIS. SEVILLA TOLD THE EMBOFF HE IS CONFIDENT THE GOE CAN OVERCOME THE OPPOSITION TO THE PRICE RISES AND IS PREPARED TO DEAL WITH ANY PROTESTERS WHO TAKE TO THE STREETS. THE EMBASSY HAS OBTAINED FROM THE MINISTRY OF NATURAL
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RESOURCES A DETAILED ACCOUNT OF HOW THE PRICE RISES WOULD BE EFFECTED; THE PLAN PARTIALLY TIES THE GASOLINE PRICE RISE TO AN INCREASE IN OCTANE RATINGS. END SUMMARY.

1. THE PUBLIC STATEMENT OF SANTIAGO SEVILLA, GOE FINANCE MINISTER, ON THE NEED TO RAISE GASOLINE PRICES WAS SUMMARIZED IN REFTEL.

2. THE INITIAL RATHER RESTRAINED REACTION TO SEVILLA'S COURAGEOUS AND INTELLIGENT STATEMENT INDICATES HE HAS SUCCEEDED IN PUTTING OPPONENTS OF THE PRICE HIKES ON THE DEFENSIVE. IN A MEETING WITH E/C COUNSELOR ON THE EVE OF THE PUBLICATION OF HIS STATEMENT, SEVILLA CONFIDED THAT HE WAS "DECLARING WAR" ON THESE GROUPS, WHICH HE DEPICTED AS CONSISTING MAINLY OF "LEFTISTS AND POLITICAL DEMAGOGUES". HE ESTIMATED THE PRESENT SUBSIDY OF DOMESTIC CONSUMPTION OF PETROLEUM PRODUCTS AT ABOUT \$200 MILLION A YEAR. HE SAID THE MILITARY REGIME IS DETERMINED TO RAISE THESE PRICES IN ONE FELL SWOOP BEFORE LEAVING OFFICE LATER THIS YEAR; THE ALTERNATIVE OF A SERIES OF PERIODIC SMALL INCREASES HAS BEEN RULED OUT, HE SAID, BECAUSE AS EACH ONE CAME DUE, THERE WOULD BE A REVIVED CRISIS OVER THE ISSUE.

3. SEVILLA'S FIGURE OF AN ANNUAL 22 PERCENT DOMESTIC CONSUMPTION RATE IS ON THE UPPER REACHES OF ANY NUMBER OF ESTIMATES. OTHER SOURCES PLACE THE ANNUAL GROWTH RATE AT 15 TO 18 PERCENT. ASSUMING HIS 22 PERCENT FIGURE IS CORRECT, AND USING THE ESTIMATED DOMESTIC CONSUMPTION OF 63,000 BPD IN 1977, TOTAL CONSUMPTION IN 1983 WOULD BE 208,000 BPD. THIS FIGURE IS ABOUT EQUAL TO THE CURRENT MAXIMUM PRODUCTION RATE OF 210,000 BPD. PROJECTED NEW PRODUCTION HOWEVER OF ABOUT 8000-10,000 BPD BY CEPACO (CITY ECUATORIANA PRODUCTION COMPANY) BEFORE THE END OF 1978, CONFIDENTIAL

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ALONG WITH THE PROBABLE DISCOVERY OF NEW RESERVES BY CEPE AND TEXACO UNDER A JOINT WORK PROGRAM IN 1978 AND POSSIBLE FUTURE PROGRAMS, WILL LIKELY RAISE PRODUCTION SUBSTANTIALLY BY 1983. THUS THERE WOULD STILL BE SIZEABLE (THOUGH REDUCED) OIL EXPORT EARNINGS EVEN IF DOMESTIC CONSUMPTION WERE UNBRIDLED.

4. RELIABLE MINISTRY OF NATURAL RESOURCES SOURCES REPORT THAT UNDER THE CURRENT FAVORED PLAN FOR HIKING PRICES, THE GOE INTENDS TO MIX THE 92 OCTANE GASOLINE WHICH IS PRODUCED AT THE NEW ESMERALDAS STATE REFINERY WITH THE 80 OCTANE GAS ALSO PRODUCED THERE. THE RESULTANT MIXTURE OF BETWEEN 82 AND 84 OCTANE GAS WOULD BE SOLD AT A PER-GALLON PRICE OF ABOUT 48 CENTS (US) COUNTRYWIDE. IN FACT, UNKNOWN TO THE GENERAL PUBLIC, THE GOE IS ALREADY SELLING THIS MIXTURE, BUT AT THE LOW 18.6 CENT-PER-GALLON PRICE. THE LOWER-

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C O N F I D E N T I A L SECTION 2 OF 2 QUITO 1357

QUALITY 63 OCTANE GASOLINE, INCREASINGLY SCARCE RECENTLY, WOULD BECOME THE RESPONSIBILITY OF THE GULF AND ANGLO REFINERIES ON THE SANTA ELENA PENINSULA. THESE TWO REFINERIES, WHOSE PRESENT COMBINED GASOLINE OUTPUT IS ABOUT 60 PERCENT 80 OCTANE AND THE BALANCE 63 OCTANE, WOULD PRODUCE EXCLUSIVELY 63 OCTANE GAS TO BE SOLD AT A PRICE OF ABOUT 40 CENTS PER GALLON. BASED ON THE CURRENT INPUT COST OF \$1.48 PER BARREL OF CRUDE SUPPLIED BY CEPE AND TEXACO, THE TOTAL COST FOR EXTRACTING, TRANSPORTING, REFINING AND MARKETING GASOLINE IS NOW JUST UNDER 32 CENTS/ GALLON, WELL ABOVE THE RETAIL PRICE. THE GOE WANTS THE RETAIL PRICE TO COVER THESE COSTS. THE PLAN WOULD THEN ADD ON ABOUT A 16 CENT TAX WHICH WOULD GO TOWARDS THE CENTRAL BUDGET, CEPE, AND INECEL (THE STATE ELECTRIFICATION INSTITUTE). FOR OTHER DERIVATIVES, THE TAX WOULD ALSO RISE ABOUT 16 CENTS. AN ESTIMATED \$80 MILLION WOULD BE RAISED BY THESE NEW TAXES (WHICH HOWEVER, WOULD BE PARTIALLY OFFSET BY A SUBSIDY PROGRAM DESCRIBED BELOW).

5. THE SPECIFICS OF THE PRICE HIKE COULD CHANGE AS THE GOE GAUGES THE DEGREE OF PUBLIC SUPPORT. IN ANY CASE, THE NATURAL RESOURCES MINISTRY HOPES TO PUT THIS HIKE INTO EFFECT BY EARLY APRIL OF THIS YEAR.
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6. THE GOE HAS PREPARED TWO ALTERNATIVE PLANS WHICH WOULD RAISE PRICES EVEN MORE. ONE WOULD RAISE THE PRICE ALLOWED TO CEPT AND TEXACO FOR CRUDE SUPPLIED FOR LOCAL CONSUMPTION TO \$3.00/BARREL (FROM THE PRESENT \$1.48), WITH

TOTAL GASOLINE PRODUCTION COSTS PER GALLON OF ABOUT 38 CENTS AND TAXES OF 16 CENTS ACCOUNTING FOR A TOTAL PRICE OF 54 CENTS. UNDER THE SECOND PLAN, THE GOE WOULD RAISE THE INPUT COST OF CRUDE TO \$5.00/BARRLE WITH TOTAL GASOLINE PRODUCTION COSTS PER GALLON OF 46 CENTS AND TAXES OF 16 CENTS EQUALLING A TOTAL PRICE OF 62 CENTS. WHILE BOTH OF THESE ALTERNATIVES WOULD RAISE THE RETURN TO CEPE, THE GENERAL PUBLIC WOULD HAVE TO COMPENSATE ALSO THE INCREASED RETURN ON TEXACO'S OPERATIONS. NEITHER OF THESE ALTERNATIVES IS LIKELY TO BE PUT INTO EFFECT FOR SOME TIME, ACCORDING TO THE NATURAL REASOURCES MINISTRY.

7. THE MINISTRY ESTIMATES THAT PUBLIC TRANSPORT ENTITIES ACCOUNT FOR ABOUT 50 PERCENT TOTAL CONSUMPTION IN THE COUNTRY, MEANING THAT THE FULL SUBSIDIES TO THESE ENTITIES WOULD REDUCE TOTAL NEW REVENUES BY ABOUT 50 PERCENT. THE PLANNED SUBSIDIES WOULD BE EFFECTED THROUGH A COUPON PROGRAM, WITH EACH COUPON ALLOWING THE BEARER TO PURCHASE A GIVEN NUMBER OF GALLONS OF GASOLINE AT THE PRESENT PRICE. A SUBSIDY RECIPIENT WOULD RECEIVE AT THE BEGINNING OF EACH MONTH A QUANTITY OF COUPONS BASED UPON PAST CONSUMPTION. EACH COUPON WOULD CONTAIN HREE PARTS; ONE PART WOULD GO TO THE MINISTRY OF GOVERNMENT & POLICE, THE EXECUTING AGENCY, ANOTHER PART THE SUBSIDY RECIPIENT WOULD HAVE TO TURN BACK TO THE MINISTRY OF GOVERNMENT BEFORE RECEIVING NEW COUPONS EACH MONTH, AND THE THIRD PART WOULD GO TO GASOLINE STATION OPERATORS WHO WOULD ALSO HAVE TO TURN THE STUBS IN TO THE

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MINISTRY OF GOVERNMENT. THE NATURAL RESOURCES MINISTRY SOURCES DECLARED THAT THE PROGRAM HAD ENOUGH BUILT-IN ADMINISTRATIVE CONTROLS TO AVOID FRAUD. THE EMBASSY BELIEVES, HOWEVER, THAT THE ECUADOREANS ARE CAPABLE OF DEVISING SCHEMES TO DEFRAUD THE SYSTEM EVEN BEFORE IT GOES INTO EFFECT. THE IDEA OF A SINGLE GASOLING PRICE WITH DIRECT FINANCIAL SUBSIDIES TO THE PUBLIC TRANSPORT ENTITIES AND INDEPENDENT DRIVERS WAS REJECTED BY THE NATURAL RESOURCES MINISTRY AS TOO CUMBERSOME AND COMPLEX.

8. SEVILLA, IN RESPONSE TO A COMMENT BY THE E/C COUNSELOR THAT A MARKET SYSTEM USING COUPONS COULD LEAD TO A BLACK MARKET, REPLIED THAT IF A PRIVATE TAXI DRIVER HAD ENOUGH ENTREPRENEURIAL SKILL TO TAKE ADVANTAGE OF THE SYSTEM, THEN THIS WOULD BE JUST ANOTHER MEANS TO DISTRIBUTE WEALTH; MORE EARNESTLY, HE SAID HE THOUGHT THIS PROBLEM WOULD ARISE BUT WOULD BE MANAGEABLE.

KEMP

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